

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

May 5, 2003

IN RE:

**RULEMAKING PROCEEDING
REGULATIONS FOR TERM
ARRANGEMENTS FOR
TELECOMMUNICATIONS SERVICES**

)
)
)
)
)
)

**DOCKET NO.
00-00702**

SECOND REPORT AND RECOMMENDATION OF HEARING OFFICER

For more than five years the Tennessee Regulatory Authority ("TRA" or "Authority") has undertaken an exhaustive review and deliberation of the contract service arrangements ("CSAs") filed by BellSouth Telecommunications, Inc. ("BellSouth"). This review has occurred in many different contexts, including rulemaking and contested case proceedings. As detailed below, this history has culminated in the current docket ("the CSA rulemaking docket") to address industry-wide practices regarding CSAs. The parties and TRA staff have expended an extraordinary amount of time and energy in this review. In addition, the General Assembly has recently addressed these issues and enacted legislation which has a significant impact on this docket.

Background

This docket finds its genesis in a regularly scheduled Authority Conference held on July 7, 1998, during which certain CSAs filed by BellSouth were under consideration. At that conference the Directors voted to open Docket No. 98-00559 (the "CSA Docket") for the

purpose of addressing the competitive effects of CSAs filed by BellSouth in Tennessee and also voted to appoint a Hearing Officer for the purpose of preparing the matter for consideration by the Directors.

Issues regarding the scope of the CSA Docket were initially addressed in the *First Report and Recommendation* ("*First Report*") filed by the Hearing Officer on January 15, 1999. In approving the *First Report* by a 2 to 1 vote, the Authority reiterated its position that the focus of the CSA Docket would be BellSouth CSAs.¹

The *Second Report and Recommendation of Pre-Hearing Officer* ("*Second Report*") in the CSA Docket was issued on March 23, 1999. In that report the Hearing Officer discussed, *inter alia*, the potential discriminatory effects of CSAs and the appropriate parameters of a CSA.² The Hearing Officer also stated in the report that, while the CSA Docket was initiated to examine only BellSouth CSAs, it was the Hearing Officer's recommendation that, through discovery, CSAs be examined on an industry-wide basis.³ The *Second Report* concluded with a recommendation that at the conclusion of such discovery these issues would be ripe for a rulemaking proceeding.⁴ The *Second Report* was approved at the regularly scheduled Authority Conference held on April 6, 1999.

The *Third Report and Recommendation of Pre-Hearing Officer* ("*Third Report*") in the CSA Docket was issued on June 1, 1999. In the *Third Report* the Hearing Officer noted that "[o]f primary concern to the parties was whether the issue of discrimination should continue to be an

¹ See *In re: Proceeding for the Purpose of Addressing Competitive Effects of Contract Service Arrangements Filed by BellSouth Telecommunications, Inc. in Tennessee*, Docket No. 98-00559, *Fourth Report and Recommendation of Pre-Hearing Officer*, p. 2 (July 8, 1999). See also *In re: Proceeding for the Purpose of Addressing Competitive Effects of Contract Service Arrangements Filed by BellSouth Telecommunications, Inc. in Tennessee*, Docket No. 98-00559, *Order Approving and Adopting Report of Pre-Hearing Officer* (January 5, 2000).

² See *id.*, *Second Report and Recommendation of Pre-Hearing Officer*, pp. 11-14 (March 23, 1999).

³ See *id.*, p. 17 (March 23, 1999).

⁴ See *id.*, p. 16.

issue in this docket.”⁵ The Hearing Officer noted further that “[t]he consensus of the parties was that the issue of discrimination as it relates to the offering of contract service arrangements, by either BellSouth or by CLECs, should be examined in the context of a rulemaking proceeding.”⁶ The *Third Report* concluded by recommending, *inter alia*, “that a rulemaking proceeding be initiated through the opening of another docket, as soon as practicable, for the purpose of promulgating rules that will address industry-wide practices of offering Contract Service Arrangements.”⁷ The *Third Report* was approved and adopted by a 2 to 1 vote at the regularly scheduled Authority Conference held on June 8, 1999.

The *Fourth Report and Recommendation of Pre-Hearing Officer* (the “*Fourth Report*”) in the CSA Docket was issued on July 8, 1999. In the *Fourth Report* the Hearing Officer recommended that the Authority open a rulemaking docket to address industry-wide CSAs. The Hearing Officer noted his previously expressed opinion that the questions regarding the appropriate parameters of a CSA and the industry-wide use of CSAs were ripe for a rulemaking proceeding.⁸ The Hearing Officer also noted the development of specific issues in the CSA Docket regarding the potential discriminatory effects of CSAs.⁹ The Hearing Officer noted further that “the rules that govern CSAs provide no criteria for identifying similarly situated customers nor any methodology for examining potentially discriminatory practices by local telecommunication service providers.”¹⁰ The *Fourth Report* concluded with several

⁵ See *In re: Proceeding for the Purpose of Addressing Competitive Effects of Contract Service Arrangements Filed by BellSouth Telecommunications, Inc. in Tennessee*, Docket No. 98-00559, *Third Report and Recommendation of Pre-Hearing Officer*, p. 3 (June 1, 1999).

⁶ See *id.*

⁷ See *In re: Proceeding for the Purpose of Addressing Competitive Effects of Contract Service Arrangements Filed by BellSouth Telecommunications, Inc. in Tennessee*, Docket No. 98-00559, *Third Report and Recommendation of Pre-Hearing Officer*, p. 5 (June 1, 1999).

⁸ See *In re: Proceeding for the Purpose of Addressing Competitive Effects of Contract Service Arrangements Filed by BellSouth Telecommunications, Inc. in Tennessee*, Docket No. 98-00559, *Fourth Report and Recommendation of Pre-Hearing Officer*, p. 12 (July 8, 1999).

⁹ See *id.*, p. 11 (July 8, 1999).

¹⁰ See *id.*, p. 12 (July 8, 1999).

recommendations, including the Hearing Officer's recommendation that the Authority open a rulemaking docket to address industry-wide CSAs.¹¹ The *Fourth Report* was approved and adopted by an order issued on February 3, 2000, and Docket No. 00-00702 subsequently commenced.

Over the next two years proposed rules regarding CSAs were written and approved by the Authority.¹² These rules were ultimately not approved by the Attorney General and did not go into effect.

On August 2, 2002, the Consumer Advocate and Protection Division ("CAPD") of the Office of the Attorney General filed its *Complaint and Petition to Intervene* ("*Intervention*") in Docket 00-00702. In its *Intervention* the CAPD focused on issues related to price discrimination stating that the CSAs under consideration in this docket "cannot be justified on the basis of general competition" and that "it must be established that unique or special circumstances exist which are necessary to approve the CSA in the first place."¹³

On August 7, 2002, the Directors voted to proceed with this rulemaking proceeding and to hold the *Intervention* in abeyance pending the outcome of the rulemaking.¹⁴

The Current CSA Rulemaking Docket

A detailed history of this proceeding was set forth in an earlier report and recommendation issued by this Hearing Officer on December 31, 2002, and, therefore, a further recitation of the past proceedings is not necessary here. During this proceeding, CSAs were filed

¹¹ See *In re: Proceeding for the Purpose of Addressing Competitive Effects of Contract Service Arrangements Filed by BellSouth Telecommunications, Inc. in Tennessee*, Docket No. 98-00559, *Fourth Report and Recommendation of Pre-Hearing Officer*, p. 10 (July 8, 1999).

¹² The terms of the former Directors of the Authority, Chairman Sara Kyle, and Directors H. Lynn Greer, Jr. and Melvin J. Malone, expired on June 30, 2002. Chairman Kyle was re-appointed and commenced a new term as a Director of the Authority on July 1, 2002. Deborah Taylor Tate, Pat Miller, and Ron Jones began terms as Directors on July 1, 2002.

¹³ *Complaint and Petition to Intervene*, pp. 2, 5 (August 2, 2002).

¹⁴ Transcript of Authority Conference, pp. 64-65 (August 7, 2002).

and reviewed by TRA staff and were allowed to take effect pending the resolution of this docket.

On August 19, 2002, the Directors appointed Director Deborah Taylor Tate to serve as a Hearing Officer to prepare the issues and a procedural schedule for a rulemaking proceeding in this docket. Soon after this Hearing Officer's appointment to the CSA Rulemaking Docket, settlement negotiations, at the request of the parties, commenced in September 2002 and for a period of time status reports were filed every two weeks. On November 25, 2002, a status conference was held and, with no settlement presented, the period for settlement negotiations was closed and oral argument was set for the second regularly scheduled Authority Conference in January 2003. The Hearing Officer requested that comments be filed and that oral remarks be presented to all four directors. The parties made presentations to the Directors on January 27, 2003, and the Authority allowed the opportunity for additional written submissions, the last of which was filed March 5, 2003. During this time, legislation concerning CSAs was introduced in the General Assembly, was passed unanimously by both houses, and was signed by Governor Bredesen into law effective April 23, 2003.¹⁵ This legislation amended the text of Tenn. Code Ann. § 65-5-201, so that it now reads as follows:

Notwithstanding any other provision of state law, special rates and terms negotiated between public utilities that are telecommunications providers and business customers shall not constitute price discrimination. Such rates and terms shall be presumed valid. The presumption of validity of such special rates and terms shall not be set aside except by complaint or by action of the TRA directors, which TRA action or complaint is supported by substantial evidence showing that such rates and terms violate applicable legal requirements other than the prohibition against price discrimination. Such special rates and terms shall be filed with the authority.

Discussion

This Agency is charged with protecting the interests of utility consumers and providers

¹⁵ The vote in the House of Representatives was 95-0; the vote in the Senate was 31-0.

while facilitating the transition to a more competitive environment.¹⁶ The changed circumstances of the telecommunications industry in Tennessee are readily apparent. Evidence is present in many areas of this industry that the competition contemplated as a public policy goal of this agency by both Congress and the General Assembly is occurring. There are thirty-eight (38) CLECs which have entered the telecommunications market and which are currently providing telecommunications services in Tennessee. CLECs operate over 515,000 of the wired lines in Tennessee with 89% of those wired lines dedicated to business services. Last year the FCC granted BellSouth the opportunity to enter long distance in Tennessee. The FCC's action took place after the TRA submitted to the FCC its recommendation that BellSouth be allowed to enter the long distance market in Tennessee. In developing its recommendation, the TRA examined the record and the facts—including the existence and prevalence of CSAs in Tennessee—and concluded that BellSouth had sufficiently opened its network to competitors supporting the recommendation that BellSouth be allowed to enter the long distance market. By their very nature, CSAs are indicative of competition. In fact, the competition specifically regarding CSAs has been characterized as being “fierce.”¹⁷ Thus, rather than evidencing the stifling of competition in the marketplace, CSAs indicate that competition in the marketplace exists.

With the entry of BellSouth in the long distance market, the TRA and the FCC recognized that conditions were ripe for competition in local telecommunications markets in Tennessee. However, there is a transition period from regulation to full competition. During this transition, the TRA must adjust its role from that of solely a regulator to that of both a regulator and a market monitor to ensure that a balance exists between competition, the consumer and the public interest.

¹⁶ See Tenn. Code Ann. § 65-4-123 (Supp. 2002).

¹⁷ Transcript of Authority Conference, p. 84 (January 27, 2003).

The new CSA law supports and continues the TRA's discretion to take action when necessary to ensure that CSAs work to improve the competitive marketplace. The role of the TRA is to monitor the behavior of market participants in order to determine if their actions hinder the development of competition and the provision of reliable, efficient and not unduly discriminatory telecommunications services and to encourage opportunities for improvement and discourage opportunities for market power abuses. This new role is consistent with the reduction of regulation prescribed by both the state and federal telecommunications acts and furthers this transition.

As evidenced by the history of the CSA Docket noted above and as presented in the first *Report and Recommendation of Pre-Hearing Officer* issued in this docket on December 31, 2002, CSAs have been the subject of almost continuous evaluation by the Authority from a contested case hearing to a show cause hearing to a multi-year rulemaking proceeding lasting more than thirty-three (33) months and encompassing over fifty-three (53) filings. Hundreds of hours of meetings, settlement negotiations and hearings by TRA Directors, staff, parties and their attorneys have been expended. Each CSA has been evaluated and reviewed by Authority Staff to meet statutory requirements as well as guidelines reflected in settlement agreements and TRA orders.¹⁸

¹⁸ The criteria utilized by Authority Staff to review BellSouth CSAs was articulated by Mr. Joe Werner, Chief of the Telecommunications Division, at the January 27, 2003 Authority Conference. There Mr. Werner stated that each CSA is reviewed to determine: whether the rates comply with the statutory price floor included in Tenn. Code Ann. § 65-5-208(c); whether the customer's name is disclosed in conformance with the Public Records Act; whether termination liability provisions are consistent with those adopted by the Authority in Docket 01-00681; whether there is an acknowledgement that the CSA is necessary to respond to competitive alternatives or competing offers; whether the CSA contains anti-competitive terms or otherwise illegal terms; whether the contract is available for resale as required by the FCC; for volume and term contracts, whether shortfall provisions do not apply in the event of early termination as ordered in Docket No. 99-00244; whether a 30-day notice consistent with TRA rules is present; and whether a summary of the CSA including rates and services offered in its tariffs is included. See Transcript of Authority Conference, pp. 107-108 (January 27, 2003).

The issues in this docket have been exhaustively discussed, argued, and briefed. Most importantly however, the General Assembly has recently spoken clearly and unanimously to many of these issues through the enactment of Public Chapter 41 amending Tennessee Code Annotated, Section 65-5-201, to establish that when special rates and terms are reached through negotiation between a public utility and a business customer such shall be presumed valid and shall not constitute price discrimination.

Recommendations

After considering the original purpose of this docket and the recent amendment of Tennessee Code Annotated, Section 65-5-201, the Hearing Officer makes the following recommendations:

1. The Authority should close Docket No. 00-00702.

This docket was originally opened in August 1998, almost five years ago. There has been ample opportunity for discussion. The parties to this proceeding have actually agreed on many of the contentious issues in this docket of late. However, the General Assembly's enactment of Public Chapter 41 has resolved the majority of the issues, including price discrimination issues, which form the foundation of this docket. The continued review of each CSA by TRA staff, the continuing opportunity for parties to intervene and the continuing general, plenary authority of the TRA are together more than sufficient to answer what few issues may remain. Taken together, all of these factors support the decision to close this proceeding. As is the case with all state agencies during this time of budget crisis, we need to focus the energies and efforts of our staff and this Agency on the issues that are before us; not those behind. Efficient, effective management demands no less. As was stated in a recent filing

in this docket: "Clearly the situation and issues that exist in today's docket are very different than that of August 1999."¹⁹

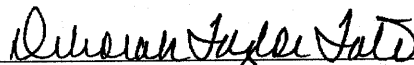
2. The Authority should place all pending CSAs which, by previous order of the Authority, have been allowed to go into effect pending the outcome of this proceeding on the next Conference Agenda for deliberation by the appropriate assigned voting panels. It is the recommendation of the Hearing Officer that, based on the closure of this rulemaking proceeding, the voting panels should allow these CSAs to go into effect.

The numerous CSAs which have been submitted during the course of this rulemaking proceeding have already been reviewed by Authority Staff and contain no terms or conditions which, in light of the recent amendment to Tenn. Code Ann. § 65-5-201, warrant suspension or non-approval.

3. The interventions pending in the above-referenced CSAs should be denied.

As noted above, the Legislature's enactment of Public Chapter 41 has resolved the majority of the issues including price discrimination issues which form the foundation of this docket. If the Directors vote to close this docket, the *Intervention*, which centered on price-discrimination issues, will be rendered moot.

Respectfully submitted,



Deborah Taylor Tate, Director
acting as Hearing Officer

¹⁹ *Consumer Advocate Rebuttal to Reply Comments of Industry Members*, p. 4 (March 5, 2003).